In the Supreme Court of the United States

OCTOBER TERM, 1943

No. 393

DURKEE FAMOUS FOODS, INC.,
Cross Petitioner,

vs.

CARTER H. HARRISON,
Collector of Internal Revenue for the
First District of Illinois,
Cross Respondent.

CROSS PETITION FOR A WRIT OF CERTIORARI
To the United States Circuit Court of Appeals
For the Seventh Circuit

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To the United States Circuit Court of Appeals,
For the Seventh Circuit.

The cross petitioner, Durkee Famous Foods, Inc., respectfully prays that a writ of certiorari issue to review that part of the judgment of the United States Circuit Court of Appeals for the Seventh Circuit entered in the above cause on June 1, 1943, as later amended, which is adverse to the cross petitioner. The cross respondent has filed in this Court a petition for writ of certiorari to review part of the same judgment and has filed a certified transcript of the record, including the proceedings in the Circuit Court of Appeals.

OPINIONS BELOW.

The opinion of the District Court (R. 426) is reported in 46 F. Supp. 642. The opinion of the Circuit Court of Appeals (R. 471) is reported in 136 F. (2d) 303.

JURISDICTION.

The judgment of the Circuit Court of Appeals was entered on June 1, 1943. (R. 486-487.) Upon motion of cross petitioner, it was amended by the Circuit Court of Appeals on August 12, 1943. The time within which to file this cross petition was extended to October 1, 1943 by an order signed by Mr. Justice Murphy on August 25, 1943. Jurisdiction of this Court is invoked under Section 240(a) of the Judicial Code, as amended. 28 U. S. C. § 347(a).

STATUTE AND REGULATIONS INVOLVED.

Part of the statute is quoted below. The entire section and the regulations are quoted in the appendix.

Revenue Act of 1934, c. 277, 48 Stat. 680:

Sec. 602½. Processing Tax on Certain Oils.

(a) There is hereby imposed upon the first domestic processing of coconut oil, sesame oil, palm oil, palm kernel oil, or sunflower oil, or of any combination or mixture containing a substantial quantity of any one or more of such oils with respect to any of which oils there has been no previous first domestic processing, a tax of three cents per pound, to be paid by the processor. * * *. For the purposes of this section the term "first domestic processing" means the first use in the United States, in the manufacture or production of an article intended for sale, of the article with respect to which the tax is imposed, but does not include the use of palm oil in the manufacture of tin plate.

QUESTIONS PRESENTED.

1. In determining the number of pounds of oil measuring the tax on the first domestic processing, does the statute require that there be included in the determination the number of pounds of substances such as water, sand, free fatty acids and dirt which are associated with the oil but which are not oil?

2. In determining the number of pounds of oil measuring the tax on the first domestic processing, does the statute require that there be included in the determination the number of pounds of oil and other substances which are lost in processing and therefore are not and never can be "used" in the manufacture or production of an article intended for sale?

3. Irrespective of the number of processings of oil, is there a "first domestic processing" of oil within the statute prior to the "first use" of the oil in the manufacture or production of an article such as margarine intended for sale?

STATEMENT.

Cross petitioner brought two actions in the United States District Court for the Northern District of Illinois, Eastern Division, for the recovery of processing taxes allegedly illegally collected by cross respondent. The actions were consolidated in the District Court (R. 49), which rendered a single judgment. (R. 445-447.) In its consolidated form the case involves four separate claims of cross petitioner.

The first claim relates to taxes paid by cross petitioner in respect of oil which had been subjected to one or more processings before the effective date of the statute. (R. 3-6.) A stipulation of counsel fixed the amount of taxes involved in this claim at $76,899.09 (R. 296) and the District Court entered judgment for cross petitioner for this amount and interest. (R. 446-447.) This part of the judgment was affirmed by the Circuit Court of Appeals and is involved in the petition for a writ of certiorari of cross respondent filed in this Court, No. 266, October Term, 1943. Cross petitioner has filed a memorandum in this Court which concedes the conflict of decisions represented in the petition of cross respondent and does not oppose the granting of a writ of certiorari.

The second claim seeks recovery of processing taxes paid between July 31, 1934 and February 28, 1936 to the extent that they represent processing taxes measured by certain substances other than oil, some of which were not even subjected to a processing. (R. 17.) Prior to any processing, the substance which cross petitioner procures for processing consists of oil in association with water, sand, fiber, husks, and other impurities (collectively called the moisture, insoluble impurities, and unsaponifiables or M. I. U. content) and certain free fatty acids. (R. 432.) The oil itself is separated from the associated free fatty acids by what is known as the neutralizing process, the first step in the refining process and admittedly a taxable processing where the refined oil is intended for sale. The water and dirt may be separated in several ways. Being heavier than oil, they will settle by gravity sooner or later to the bottom of the tank. (R. 92.) They may be dissociated by filtering the crude oil through Fuller's earth or bone char (R. 91, 147), a process which has been held not to be a taxable processing. The more efficient commercial process, the neutralizing process employed by cross petitioner, involves the addition of a caustic to the crude oil and agitation of the mixture, as a result of which a substantial portion of the M. I. U. content and the bulk of the free fatty acids are separated from the oil. (R. 91, 126, 127, 433.)

Expert witnesses who testified in the District Court agreed that no part of the M. I. U. content or the free fatty acids constitutes "oil" as the word is generally understood (R. 86, 136, 146, 179-180), but despite Article 5 of Treasury Regulations 48 which provides that the measure of the tax is the number of pounds of "oil" put into process, cross petitioner was required to compute and pay the tax not only upon the number of pounds of oil but upon the number of pounds of M. I. U. content and free fatty acids which entered the neutralizing process. Its claim for refund of

taxes to the extent that they represented taxes measured by these substances which are not oil was rejected by the Commissioner of Internal Revenue. (R. 28-29, 34-35.) The District Court entered judgment[1] for cross petitioner on this claim (R. 445-446) but the Circuit Court of Appeals reversed.

The third claim concerns processing taxes paid between July 31, 1934 and February 28, 1936 with respect to oil which was not and never could be used in the manufacture or production of an article intended for sale because the oil was lost in processing. In the usual case the crude oil is subjected to three or four processings—neutralizing, washing, bleaching and deodorizing. (R. 87, 145, 180.) Due to various causes, among them absorption and cohesion with other substances, there is a loss of oil in these various operations (R. 95-97, 145, 180), a loss which in the trade is called a shrinkage loss. (R. 180.) Although the oil involved in the shrinkage loss was not and never could be used in the manufacture or production of an article intended for sale, cross petitioner was required to pay processing taxes with respect to it which the Commissioner subsequently refused to refund. (R. 28-29, 35-37.) The District Court entered judgment against cross petitioner dismissing this claim (R. 446) and the Circuit Court of Appeals affirmed.

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[1] The amount of the judgment entered for cross petitioner was computed by reference to a bill of particulars (R. 47) filed by cross petitioner at the request of cross respondent. (R. 80-81.) The bill of particulars did not separately disclose the amount of free fatty acids and unsaponifiable substances, and in consequence the judgment did not include the amount of taxes assessed and paid because the acids and unsaponifiable substances were included in the measure of the tax. (R. 292.) Leave to amend the bill of particulars and complaint to itemize these substances separately was denied by the District Court (R. 295), and although cross petitioner assigned error with respect to this ruling (R. 456), the Circuit Court of Appeals refused to consider the contention (R. 482) in view of its decision on the merits.

The fourth claim involves processing taxes paid between July 31, 1934 and February 28, 1936 upon the use of oil in the production of an article (i.e., refined oil) which was not intended for sale and was not actually sold. (R. 20-21.) Some of the crude oil is subjected to three or four processings and is then sold as refined oil to various manufacturers. (R. 97, 103-104, 136.) But some of the oil is subjected to a fifth or hydrogenating process which is the first processing or use of oil in the manufacture or production of food products such as margarine, intended for sale, and is then used by cross petitioner in the manufacture of such food products. (R. 102, 156-157, 436.) Despite the foregoing undisputed facts, cross petitioner was required to pay processing taxes in respect of the use of this oil. The Commissioner denied cross petitioner's claim for refund (R. 28-29, 35-37), the District Court entered judgment dismissing it (R. 446), and the Circuit Court of Appeals affirmed. This claim involves a portion of the taxes involved in the second and third claims and presents, as to this portion, an additional ground of recovery.

In disposing of cross petitioner's four claims, the Circuit Court of Appeals originally entered two judgments. (R. 486-487.) Upon motion of cross petitioner a single judgment was substituted.

SPECIFICATIONS OF ERROR TO BE URGED.

The Circuit Court of Appeals erred:

1. In holding that the M. I. U. content and the free fatty acids are to be included in determining the number of pounds of oil which measures the processing tax imposed by the statute.

2. In holding that oil which is lost in processing and is not and never can be used in the manufacture or production of an article intended for sale is to be included in determining the number of pounds of oil which measures the processing tax imposed by the statute.

3. In holding that, in determining the number of pounds of oil which enters the first or neutralizing process and which measures the processing tax imposed by the statute, there must be included the number of pounds of oil used in the manufacture or production of an article which is not intended for sale and is not sold.

4. In failing to consider and reverse the ruling of the District Court overruling cross petitioner's motion for leave to amend its bill of particulars and, to the extent necessary, its original complaint.

5. In failing to consider and adopt the interpretation of the word "oil" in the statute which represents the general understanding of persons engaged in the business of processing the oils taxed by the statute and of the five expert witnesses who testified at the trial in the District Court.

6. In entering judgment for cross respondent and in failing to enter judgment for cross petitioner for the entire amount, with interest, demanded in the original complaint involved in this cross petition.

REASONS FOR GRANTING THE WRIT.

The Circuit Court of Appeals has erroneously decided three important questions relating to the proper construction of Section 602½ of the Revenue Act of 1934, and in deciding them adversely to cross petitioner has sanctioned an administrative interpretation which is not only wholly in conflict with the intention and express language of the statute but in part is refuted by a subsequent amendment to the statute enacted by Congress in 1936 and is inconsistent with another administrative interpretation relating to the same statute. The quesions raised by cross petitioner are questions of *first* impression and, with the exception of the questions relating to cross petitioner's claims involving the inclusion of salts and free fatty acids, are of continuing

importance in the administration of this statute and are inherent in Section 2470 of the Internal Revenue Code. There are three cases presently pending in federal courts in Ohio which involve one or more of these same questions, the answer to which is of great importance to every company in the United States engaged in the business of processing the oils specified in the statute.

The judgment of the Circuit Court of Appeals dismissing cross petitioner's fourth claim is in direct conflict with the decision of the Circuit Court of Appeals for the Third Circuit in the case of *Colgate-Palmolive-Peet Co. v. United States,* 130 F. (2d) 913. The nature of this conflict is explained in part 3 of the argument which follows. The construction by the Circuit Court of Appeals of the word "oil" in the statute is completely contrary to the understanding of its meaning held by persons engaged in the processing of oils taxed by the statute and to the undisputed evidence of the five expert witnesses who testified at the trial in the District Court.

In addition, the holdings of the Circuit Court of Appeals which are adverse to cross petitioner are embraced in a single judgment in consolidated actions which should be reviewed in its entirety. Another part of this judgment is involved in the petition for writ of certiorari, No. 266, October Term, 1943, which has been filed in this Court by cross respondent and which cross petitioner is not opposing.

ARGUMENT.

1. M. I. U. Content and Free Fatty Acids.

Oil is a compound of glycerin and fatty acids, and is one of the constituents of crude oil. Crude oil is a conglomerate of oil, water, sand, fiber, husks, free fatty acids, and other impurities. The uncontroverted evidence offered at the trial in the District Court makes it perfectly clear that the word "oil" does not mean oil plus other substances either in ordinary parlance or to experts who are connected

with the study and processing of oils. In the absence of convincing evidence to the contrary, it must be assumed that in enacting a statute relating to the processing of oils Congress intended the words of the statute to have the meaning ordinarily assigned to them by persons engaged in or associated with the processing of oils. Cf. *Binns v. Lawrence*, 12 How. 9.

The language of Section 602½ speaks for itself and is susceptible of only one construction, the construction of tradesman, scientist and lexicographer. The statute does not impose a tax on the processing of water, sand, free fatty acids, or dirt, nor does it impose a tax on the processing of crude oil. It imposes a tax on the processing of "oil", and Article 5 of Treasury Regulations 48 implements this provision by specifying that the measure of the tax is the quantity in pounds of "oil or oils" put into process. Proof that Congress never thought it had done more than this is the amendment to Section 602½ by Section 702[2] of the Revenue Act of 1936 (Act of June 22, 1936, c. 690, 49 Stat. 1648) which amended Section 602½ and for the first time provided for a tax on the processing of salts and fatty acids. This amendment was plainly unnecessary if salts and fatty acids were included in the word "oil" in the original section. It is equally plain that the amendment was not intended merely to clarify the scope of the original term "oil", for this explanation involves the irrational con-

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[2] § 702. "There is hereby imposed upon the first domestic processing of coconut oil, palm oil, palm-kernel oil, fatty acids derived from any of the foregoing oils, salts of any of the foregoing * * * a tax of 3 cents per pound to be paid by the processor, but the tax under this section shall not apply (1) with respect to any fatty acid or salt resulting from a previous first domestic processing taxed under this section * * *."

The exemption does not imply that fatty acids were previously included in the measure of the tax. This exemption was quite evidently intended to make sure that the new tax on the processing of fatty acids would not be imposed on fatty acids "resulting" from a previously fully taxed first domestic processing of oil prior to the effective date of Section 702.

clusion that, while there may have been doubt that "oil" includes salts and fatty acids, there was no doubt that "oil" includes sand, husks, dirt and fiber. If Congress had intended to tax the processing of "crude" oil, it certainly would have said so for it is familiar with the distinction. See Revenue Act of 1934, c. 277, 48 Stat. 680, Sec. 604. So is the Treasury Department. See S. T. 758, XIII-2 C. B. 390; S. T. 800, XIV-1 C. B. 396; S. T. 808, XIV-1 C. B. 396.

In fact, the latter agrees that dirt, fiber, husks, etc. are not to be included in the measure of the tax if they are removed by the method of filtering the crude substance through bone char or Fuller's earth, and in S. T. 808, XIV-1 C. B. 396 it is held that this removal does not constitute a "first domestic processing." Since filtering by mechanical means and neutralizing have the same object—dissociation of the oil and foreign substances—this ruling is basically at odds with the decision of the court below and with Article 5 of Treasury Regulations 48 as applied to cross petitioner, in that the tax which cross petitioner was required to pay was measured by the weight of oil plus the weight of foreign substances associated with it at the inception of the neutralizing process. This difference in tax consequences, depending upon the method of eliminating foreign substances which are not oil, can easily and properly be avoided if the statute is construed to levy what it purports to levy, a tax on the processing of *oil*, not *crude* oil or oil plus other substances which are not oil.[3]

This construction of the statutory word "oil" is not altered nor is the reach of Section 602½ extended to the

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[3] It should be noted that there are two additional reasons why the moisture and impurities may not be included in the measure of the tax. As will more fully appear in part 2 and part 3 of the argument, a "first domestic processing" is the first use of the oil in the manufacture or production of an article intended for sale. The moisture and impurities are never "used," and are never an ingredient, or an aid in the manufacture or production, of an article intended for sale. (R. 433.)

M. I. U. content and free fatty acids involved here merely because the statute speaks of "any combination or mixture containing a substantial quantity of any one or more of such oils". On its face this language implies that the combination or mixture contemplated is a combination or mixture of oils, not a combination or mixture of oil and substances which are not oil. This interpretation is supported by the testimony in the District Court (e.g., R. 139-140) that crude oil, oil in association with other substances, is not a combination or mixture as the terms are generally understood by persons engaged in the study or processing of oils. Examination of committee reports accompanying the Revenue Act of 1934 leaves little doubt that the phrase quoted above was intended to prohibit evasion of the tax by mixing or combining oils prior to importation and was intended to relate to combinations or mixtures of *oils*. See H. Rep. No. 704, 73d Cong., 2 Sess., 1939—1 C. B. 585, Part 2; S. Rep. No. 558, 73d Cong., 2d Sess., 1939—1 C. B. 625, Part 2.

2. Oil Lost in Processing.

Section 602½ contains its own definition of the phrase "first domestic processing". This definition limits the applicability of these words, and hence of the statute, to the "first use" in this country of oil the processing of which is taxed. It follows that oil which is not the subject of any "use" may not be included in the measure of the tax for otherwise the statute is given content and scope which its express language denies. Undisputed testimony established (R. 91, 95-96, 98-99, 143, 146, 180) and the District Court found (R. 435) that oil is lost in processing. It is quite evident that oil which is lost and never capable of use in the manufacture or production of an article intended for sale cannot be the subject of a "first use" within Section 602½ and Article 1(k) of the Regulations. By the Treasury Department's own test, the lost oil is excluded

from the measure of the tax since it is not and never can be "a component or constituent or ingredient of the article, or * * * a means or aid in the manufacture or production of the article" intended for sale.

3. Oil Not Intended for Sale.

The definition of "first domestic processing" in Section 602½ imposes still another limitation on the scope of the statute in addition to the limitations considered above. The collector may not assess the tax until there is a "first use" of the oil in the manufacture or production of an "article intended for sale". Conversely, the first or fifth processing of oil may not be taxed if it is not the "first use" in the manufacture or production of an "article intended for sale", whether this is because the oil is lost in processing or because the processing results only in an article which cross petitioner ships to another of its plants, subject to further processing, and then uses in the manufacture of certain food products. It is true and cross petitioner has never denied that the neutralizing process constitutes the first use of oil in the manufacture or production of an article intended for sale to the extent that the resulting refined oil is intended to be sold. But the undisputed evidence discloses (R. 102, 156-157) and the District Court found (R. 436) that some of this oil is not intended to be sold, and to this extent the tax which cross petitioner was required to pay was improperly measured by the number of pounds of oil entering the neutralizing process.[4]

Without resort to extrinsic aids to interpretation, this much would seem to be clear enough from the express language of the statute, at least if the phrase "article intended for sale" is to be given any effect at all. Reference

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[4] This is not an argument that cross petitioner should escape part of the tax. Its imposition is merely postponed to the first use of the oil in the manufacture or production of food products intended for sale.

to the background of the statute removes any doubt that Congress intended the tax to fall upon the first use of oil in the manufacture or production of an article intended for sale. An amendment offered by Senator Harrison to the proposed revenue act sought to define "first domestic processing" in Section 602½ as the "first use" of oil in the manufacture or production of an article "intended for sale, or *intended for further manufacture*" (see Cong. Rec. 73rd Cong., 2d Sess., Vol. 78, Part 6, page 6324), but the amendment was rejected (see Id., p. 6392), an unmistakable indication that Congress deliberately distinguished the first processing of oil intended for sale from the first processing of oil intended to be used in further processing or manufacture. It follows that the judgment of the Circuit Court of Appeals erroneously denied a refund to cross petitioner of processing taxes measured by the number of pounds of oil entering the neutralizing process which was not intended to be sold but was destined for further processing and manufacture.

Cross petitioner recognizes that this contention is partially inconsistent with the major premise of its first claim, the claim for refund involved in the petition for writ of certiorari, No. 266, October Term, 1943, filed by cross respondent. Some of the oil involved in that claim had not been subjected, prior to the effective date of Section 602½, to the hydrogenating process which is the first use of the oil in the manufacture or production of margarine intended for sale. Thus, if cross petitioner is correct in its contention that in respect of the oil in this category there is not a "first domestic processing" within the statute until the hydrogenating process, there was a taxable processing when the oil was hydrogenated after the effective date of Section 602½. In *Colgate-Palmolive-Peet Company v. United States,* 130 Fed. (2d) 913, the Circuit Court of Appeals for the Third Circuit held that the term "first domestic processing" means the first processing after the

effective date of Section 602½ whether in point of fact that be the first or neutralizing process, or the fifth or hydrogenating process. This decision is in direct conflict with the decision of the court below dismissing cross-petitioner's fourth claim, the one now under discussion. In the instant case the District Court (R. 437) and the Circuit Court of Appeals (R. 483) held that determination of the first claim in favor of cross-petitioner precluded a holding in its favor on the fourth claim, reasoning that if the phrase "first domestic processing" refers only to the first processing in point of fact, it cannot at the same time refer to the fifth or hydrogenating process. In consequence, the decision by the court below dismissing cross-petitioner's fourth claim constitutes a holding that the phrase "first domestic processing" means only the first processing of the oil in point of time and is, therefore, in direct conflict with the holding in the *Colgate* cases.

CONCLUSION.

The express language of the statute, the general understanding of persons engaged in the study and processing of oils, the uncontroverted evidence, the findings of fact of the District Court, and the legislative background and subsequent history of the statute combine to demonstrate that the Circuit Court of Appeals erroneously decided against the cross petitioner on each of the three claims involved in this cross petition. This cross petition should be granted and the judgment, part of which is involved in a petition filed by cross respondent, should be reviewed in its entirety.

Respectfully submitted,

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APPENDIX.

Revenue Act 1934, c. 277, 48 Stat. 680:

SEC. 602½. PROCESSING TAX ON CERTAIN OILS.

(a) There is hereby imposed upon the first domestic processing of coconut oil, seasame oil, palm oil, palm kernel* oil, or sunflower oil, or of any combination or mixture containing a substantial quantity of any one or more of such oils with respect to any of which oils there has been no previous first domestic processing, a tax of 3 cents per pound, to be paid by the processor. There is hereby imposed (in addition to the tax imposed by the preceding sentence) a tax of 2 cents per pound, to be paid by the processor, upon the first domestic processing of coconut oil or of any combination or mixture containing a substantial quantity of coconut oil with respect to which oil there has been no previous first domestic processing, except that the tax imposed by this sentence shall not apply when it is established, in accordance with regulations prescribed by the Commissioner with the approval of the Secretary, that such coconut oil (whether or not contained in such a combination or mixture), (A) is wholly the production of the Philippine Islands or any other possession of the United States, or (B) was produced wholly from materials the growth or production of the Philippine Islands or any other possession of the United States, or (C) was brought into the United States on or before the 30th day after the date of the enactment of this Act or produced from materials brought into the United States on or before the 30th day after the date of enactment of this Act, or (D) was purchased under a bona fide contract entered into prior to April 26, 1934, or produced from materials purchased under a bona fide contract entered into prior to April 26, 1934. All taxes collected under this section with respect to coconut oil wholly of Philippine production or produced from materials wholly of

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* So in original.

Philippine growth or production, shall be held as a separate fund and paid to the Treasury of the Philippine Islands, but if at any time the Philippine Government provides by any law for any subsidy to be paid to the producers of copra, coconut oil, or allied products, no further payments to the Philippine Treasury shall be made under this subsection. For the purposes of this section the term "first domestic processing" means the first use in the United States, in the manufacture or production of an article intended for sale, of the article with respect to which the tax is imposed, but does not include the use of palm oil in the manufacture of tin plate.

Revenue Act of 1936, c. 690, 49 Stat. 1648, 1742.

SEC. 702. PROCESSING TAX ON CERTAIN OILS.

(a) The first sentence of section 602½ of the Revenue Act of 1934 is amended to read as follows:

> "(a) There is hereby imposed upon the first domestic processing of coconut oil, palm oil, palm-kernel oil, fatty acids derived from any of the foregoing oils, salts of any of the foregoing (whether or not such oils, fatty acids, or salts have been refined, sulphonated, sulphated, hydrogenated, or otherwise processed), or any combination or mixture containing a substantial quantity of any one or more of such oils, fatty acids, or salts, a tax of 3 cents per pound to be paid by the processor, but the tax under this section shall not apply (1) with respect to any fatty acid or salt resulting from a previous first domestic processing taxed under this section or upon which an import tax has been paid under section 601 (c) (8) of the Revenue Act of 1932, as amended, or (2) with respect to any combination or mixture by reason of its containing an oil, fatty acid, or salt with resepect to which there has been a previous first domestic processing or upon which an import tax has been paid under such section 601 (c) (8)."

* * * * *

Treasury Regulations 48, promulgated under the Revenue Act of 1934:

ARTICLE 1. *Definitions.*—When used in these regulations, the term—* * *.

(g) Oil or *oils* means coconut oil, sesame oil, palm oil, palm kernel oil, sunflower oil, or any combination or mixture containing a substantial quantity of any one or more of such oils with respect to any of which oils there has been no previous first domestic processing. "Combination or mixture" means an article in the formation of which any of the oils have been blended, conjoined, united, admixed, combined, amalgamated, embodied or merged, either by chemical or mechanical means, with or without the presence of any other substance, and which retains a substantial portion (10 per cent or more) of substantially all the essential components of any of the oil or oils entering into such combination or mixture. It includes articles in which any of the oil or oils have been subjected to preliminary processing outside the United States or before the effective date, or both, and in which substantially all of the components of such oil or oils are present, even though the oils themselves may no longer exist as such. "Substantial quantity" means ten (10) per cent or more, by weight, of the combination or mixture.

(h) Article processed wholly or in chief value from an article with respect to which a tax is imposed means any article made entirely from oil or oils, or any article made of two or more components, the oil or oils constituting a component having a value greater than that of any other component. An article is made from an oil or oils when the oil or oils, or any of their processed forms, have been used in making the article. In determining the value of the oil or oils as a component, the combined values of the oil or oils, and of every processed form thereof used in making the article, shall be the value of the oil or oils as a component.

(i) Effective date means May 10, 1934, beginning at 11:40 a. m., eastern standard time, at which time the tax became effective.

(j) Processing means the use of the oil or oils in the manufacture or production of an article intended for sale.

(k) Use has a very broad meaning. The term includes, among other things, the using or making use of, or employing, any one or more of the oils, or any combination or mixture of the oils, in any process, or any stage or step in the manufacture or production of an article intended for sale, and includes the manufacture or production of such article in its entirety, whether such oil is used as a component or constituent or ingredient of the article, or is used merely as a means or aid in the manufacture or production of the article, and not as a component or constituent or ingredient. Examples which are in no measure all inclusive of the *use* contemplated are:

(1) Bleaching, neutralizing, refining, deodorizing, hydrogenating, sulphonating, "twitchellizing," polymerizing, saponifying, or any other commercial processing or any combination of these commercial processings, if such process or combination of processes produces an article intended for sale.

(2) The entire process of manufacture or production of an article intended for sale, where any one or more of the above-enumerated processes are but incidental steps or stages in a continuous course of manufacture or production of the article.

(3) The manufacture or production of an article intended for sale from an oil or oils upon which any of the processes enumerated in (1), above, have been performed either (A) prior to the importation of the particular oil, or (B) prior to the effective date of the Act.

(4) The use of the oil or oils in connection with any process or stage of the manufacture or production of an article intended for sale, even though the oil is not consumed therein or does not become a component

material of the article so produced. But such a use of palm oil, by the processor, in the manufacture of tin plate is specifically excepted by the Act.

(l) First domestic processing means the first use in the United States on or after the effective date of the Act. At all times in these regulations, the term *processing* or *first domestic processing* will be deemed to be synonymous with "use" or "first use in the United States on or after the effective date," respectively, and will include the meanings implied in the latter terms by subdivision *(k)*, above.

ART. 2. *Nature of the tax.*—The tax is an excise, not a property tax. It is laid not upon the oils as such, or upon the sale of such oils, but only upon their *use*.

ART. 3. *Imposition of the tax.*—The tax is imposed only on the first domestic processing on or after the effective date of the Act. However, no tax is imposed on the use of palm oil, by the processor, in the manufacture of tin plate.

ART. 4. *When tax attaches.—(a)* The tax attaches upon the first domestic processing of the oil. If some part of the processing of a particular quantity of oil takes place on or after the effective date, the tax attaches notwithstanding that some part of the processing of such quantity took place before the effective date.

(b) If oil has been subjected to any of the processes, either prior to the importation of such oil or prior to the effective date, or both, the tax attaches to the first domestic processing of such oil, after the effective date, in the manufacture or production of an article intended for sale.

ART. 5. *Measure of the tax.*—The measure of the tax is the quantity of oil or oils (in pounds) put into process, that is, the amount of tax will be determined by the quantity of the oil or oils which, in any way, enters into the first domestic processing. If oil or oils which have been processed and upon which the tax has been paid are combined with oil

or oils upon which no tax has been paid, the measure of the tax on the processing of the combination or mixture so produced is the total quantity (in pounds) of such combination or mixture.

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CITATIONS

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In the Supreme Court of the United States

OCTOBER TERM, 1943

No. 393

DURKEE FAMOUS FOODS, INC., PETITIONER

v.

CARTER H. HARRISON, COLLECTOR OF INTERNAL REVENUE FOR THE FIRST DISTRICT OF ILLINOIS

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SEVENTH CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

OPINIONS BELOW

The opinion of the District Court (R. 426–445) is reported at 46 F. Supp. 642. The opinion of the Circuit Court of Appeals (R. 471–486) is reported at 136 F. 2d 303.

JURISDICTION

The judgments of the Circuit Court of Appeals were entered June 1, 1943 (R. 486–487). A clarifying amendment, which also consolidated the two judgments into a single judgment, was entered by the Circuit Court of Appeals August 12, 1943

(R. 489–490). The time within which to file a petition for certiorari was extended to October 1, 1943, by an order of a Justice of this Court entered August 25, 1943. The petition was filed September 29, 1943. The jurisdiction of this Court is invoked under Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTIONS PRESENTED

1. Whether the tax imposed by Section 602½ of the Revenue Act of 1934 is measured upon the total quantity of oil which enters into the first domestic processing, including the so-called M. I. U. content and the free fatty acids, or whether the tax is measured upon that quantity of oil less the M. I. U. and free fatty acids removed during the processing.

2. Whether a processor who neutralizes, washes, bleaches, and deodorizes oils with respect to which the tax is imposed by Section 602½ of the Revenue Act of 1934, and who, as required by the Act, has paid the tax upon the first domestic processing, in this case the neutralizing process, is entitled to an allowance for oil lost during all or any of these processings.

3. Whether, in the case of a processor who neutralizes, washes, bleaches, and deodorizes the oils designated by Section 602½ of the Revenue Act of 1934 and who further processes the resulting oils in the preparation of food products, the tax-

able first domestic processing is the neutralizing process or is the first process which follows the deodorizing process.

STATUTES AND REGULATIONS INVOLVED

The statutes and regulations involved are set forth in the Appendix, *infra,* pp. 13–15.

STATEMENT

The taxpayer, Durkee Famous Foods, Inc., was engaged during the period May 1934 to January 1936, inclusive, in processing coconut oil, palm kernel oil, sesame oil, and sunflower oil at its various plants (R. 16, 33, 38, 84, 296–297). The taxpayer brought two separate suits in the District Court for the Northern District of Illinois for the refund of taxes paid with respect to the processing of these oils under Section 602½ of the Revenue Act of 1934 (R. 2–13, 16–38). The first suit involved the issue of statutory construction presented by *Colgate-Palmolive-Peet Co.* v. *United States,* Nos. 38 and 39, this Term, namely, whether the statutory "first domestic processing" means the first occurring after the effective date of the Act. The second suit, with which we are here concerned, involved several distinct issues. Although the cases were consolidated for trial (R. 49), the issue involved in the first suit was submitted on a stipulation of facts (R. 296–297) and presented only the question of statutory construction referred to, while the issues of the sec-

ond suit were submitted on voluminous documentary and oral evidence and presented numerous questions of both fact and law. The District Court decided for the taxpayer on the issue of the first suit and for the Collector on two of the three principal issues of the second suit (R. 426–445). On appeals by both parties, the Circuit Court of Appeals affirmed as to the first suit and as to the two issues decided in the Collector's favor in the second suit and reversed as to the issue decided in the taxpayer's favor in the second suit (R. 471–486).

The issues presented by the petition for certiorari involve a part of the taxes paid with respect to the processing of some 172,000,000 pounds of coconut oil, palm kernel oil and sesame oil (R. 46–47, 84, 201, 329–425). All of these oils were subjected to the neutralizing, washing and bleaching processes (R. 89, 94–96), taxes having been paid upon the total weight of the oil which entered the first domestic processing, that is, as applied to these oils, the neutralizing process (R. 46–47, 269). A part of the total quantity of approximately 172,000,000 pounds of these oils was sold by the taxpayer at the end of the bleaching process, to manufacturers of pharmaceuticals, cosmetics, and soaps (R. 97). The remainder of the total poundage was subjected by the taxpayer to a fourth operation, known as the deodorizing process (R. 97–98). A second part of the poundage

was sold by the taxpayer at the end of the deodorizing operation to manufacturers of food products (R. 99, 160–161). The balance was further processed by the taxpayer in the preparation of margarine, shortening, and a hard butter for the confectionery trade (R. 46–47, 160–161). The quantities of oil which were sold by the taxpayer and which were retained by it for further processing depended wholly upon market conditions at the time (R. 160).

From the chemist's standpoint, coconut oil, palm kernel oil, and sesame oil consist solely of glycerine and fatty acids in chemical combination (R. 136–137, 179, 247–254, 260–263, 323, 325, 327). As extracted from copra, palm kernels, and sesame seed, respectively, these oils customarily contain a very small percentage of fiber, hair, sand, moisture, etc., known collectively as the M. I. U. content (R. 85, 99–101, 114–116, 205). They also contain free fatty acids in quantities ranging from 5% to 6% in the case of coconut oil and palm kernel oil to about 1% in the case of sesame oil (R. 116–117). These "free" fatty acids are to be distinguished from the fatty acids which are found in chemical combination with the glycerine. Also from the chemist's standpoint, each of these oils, as extracted from copra, palm kernels, and sesame seed, constitutes a "mixture" (R. 117–123, 141, 192, 222).

In the neutralizing process a measured quantity of a caustic, sodium hydroxide, is added to the

oil and reacts with the free fatty acids to form a soap. This results in the separation and removal of most of the free fatty acids, together with about 55% of the so-called M. I. U. content of the oil (R. 89–91, 125–127). The neutral oil—that is, the original oil less most of the free fatty acids and the 55% of the M. I. U. content—is drawn off and subjected to the various succeeding processes (R. 94–99). The remaining 45% of the M. I. U. content, consisting of unsaponifiable substances such as alcohols, resinous matter, gums, etc., remains in the oil throughout the succeeding processes and as sold to the ultimate consumer (R. 126–127). Traces of free fatty acids (between .025% and .05%) also remain in the oil during the subsequent processes (R. 138, 159). If the oil is permitted to stand a substantial period of time following the neutralizing process, free fatty acids will again form due to the deterioration of the oil molecules (R. 159, 185).

It is possible to remove a part of the M. I. U. content of the oils by permitting it to settle out over a period of time; this method is impracticable (R. 92). It is also possible to remove a part of the M. I. U. by the treatment of the oils with bone char and Fuller's earth (R. 91). This method, however, does not remove the free fatty acids (R. 152).

During the neutralizing process, as well as during the washing, bleaching and deodorizing processes, there inevitably occur losses of oil, which

in small quantities settles out with the free fatty acids, sticks to the side of the vat, drains out through leaky valves, is carried away with the water during the washing process, is absorbed by the bleaching ingredient during the bleaching process, or is carried away with the steam during the deodorizing process (R. 91, 95, 96, 98–99, 149). The amount of the oil lost during these processes varies with the efficiency of the operations (R. 190–191).

ARGUMENT

The Collector has filed a petition for certiorari (No. 266, this Term) from the portion of the judgment of the Circuit Court of Appeals which is adverse to him. That petition presents only a question of statutory construction, on stipulated facts, which was decided by the court below in a manner squarely contrary to the decision of the Circuit Court of Appeals for the Third Circuit in *Colgate-Palmolive-Peet Co.* v. *United States,* 130 F. 2d 913 (Nos. 38 and 39, this Term). The present petition, on the other hand, involves several issues wholly distinct from the single issue presented in the Collector's petition. As to these issues, there is no conflict and the decision of the Circuit Court of Appeals was right. We accordingly believe that the present petition should be denied.

1. The oils here involved customarily contain, prior to processing, minute quantities of waste

matter, known as the M. I. U. content, as well as free fatty acids. During the course of the neutralizing operation about half of these waste materials and substantially all of the free fatty acids are removed. Section 602½ of the Revenue Act of 1934 (Appendix, *infra,* pp. 13–14) imposes a tax, not upon the oils as such, but upon their first domestic processing. Consistently with the statute, the regulations have always provided that the measure of the tax is the quantity of oil or oils put into processing. Treasury Regulations 48, Article 5 (Appendix, *infra,* p. 15). Under this issue, the taxpayer does not dispute that the neutralizing processing was properly the first domestic processing. Thus, in arguing that the measure of the tax should exclude the materials removed during the course of neutralizing (Pet. 8–11), the taxpayer in effect is contending that the measure of the tax is the oil which *results from* rather than *enters into* the taxable processing. This, and the several supporting arguments designed to secure this result, conflict with the statute. Moreover, the 1936 amendment (Appendix, *infra,* pp. 14–15), contrary to taxpayer's assertion (Pet. 9–10), strongly supports the Collector's position that the tax is measured upon the total quantity of oil entered into processing, including the customary and usual constituents of the oil. The 1936 amendment for the first time taxed the independent processing of the fatty acids. In so extending the tax Congress recognized, however,

that fatty acids "resulting from" a previous processing taxable under the 1934 Act would already have paid a tax. Accordingly, in order to avoid double taxation, it expressly excluded such fatty acids from the 1936 tax. This understanding of the scope of the 1934 tax is inconsistent with the taxpayer's contention that it should be restricted so as to exclude from its measure the free fatty acids and the other materials which, strictly from a chemist's standpoint, are not oil. The Circuit Court of Appeals correctly held for the Collector on this issue.

2. The taxpayer also contends (Pet. 11–12) that it is entitled to an allowance for oil lost during the neutralizing and subsequent processings. But such losses, which are in extremely small amounts and vary with the efficiency of the operations, all occurred subsequent to the taxable event—the entry of the oil into the first domestic processing. Section 602½ (c) and (d) of the Revenue Act of 1934 allow, in two instances, credit or refund of processing taxes paid, based upon the subsequent disposition of the oil. No such credit or refund is provided as to oil lost subsequent to the taxable event. The taxpayer rather clearly is arguing for an allowance which the statute fails to give. On this, as well as the third issue, both courts below correctly held for the Collector.

3. A "domestic processing," under Section 602½, is a "use" of the oils "in the United

States, in the manufacture or production of an article intended for sale." Some of the oils were neutralized, washed, bleached, and deodorized, and, depending upon market conditions at the time, were further processed by the taxpayer in the preparation of margarine and other food products, which were then sold. As to these oils, taxpayer argues in effect (Pet. 12–14) that there was no "domestic processing" until the processing following the deodorizing processing, on the ground that until then there was no "use" of them in the production of an article (margarine, etc.) intended for sale. The practical importance of this contention is that if the tax can be postponed to the later processing, the removable M. I. U. and free fatty acids will have been eliminated and the measure of the tax reduced. The distinction which taxpayer seeks to draw, however, is baseless, since the neutralizing, washing, bleaching, and deodorizing operations, no less than the subsequent processings, are essential to the production of margarine and the other food products. The statute probably meant to distinguish only between an industrial use and a home use of the oils; certainly the taxable event, when the conditions are otherwise satisfied, does not turn on the *subsequent* use made of the oils, for if this were so the event frequently could not be determined until long after the tax was due. The amendment referred to (Pet. 13) was directed

to an entirely different matter—the tax free processing of certain quantities of Philippine coconut oil—and was rejected without mention of the instant question. Cong. Rec., Vol. 78, Part 6, pp. 6308–6324, 6392.

The taxpayer claims (Pet. 13–14) a conflict on this point between the decision of the courts below and that of the Circuit Court of Appeals for the Third Circuit in the *Colgate* case, *supra*. The claim is unwarranted. This question was neither tendered to, nor decided by, the Third Circuit. The *Colgate* issue, like the issue presented in the Collector's petition for certiorari in No. 266, assumes, in accordance with the stipulation of the parties, that there was a "domestic processing" of the oils both before and after the 1934 Act. The question there is whether, notwithstanding a previous domestic processing, the first domestic processing after the effective date of the Act is taxable.[1]

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[1] It is true that, although the Collector's position is consistent throughout, the taxpayer's position as to the meaning of "domestic processing," under 3, *supra*, is inconsistent with its underlying position on the issue presented in No. 266. This inconsistency was recognized and dealt with by a stipulation of the parties in the District Court (R. 72–73, 231–233). But it is an inconsistency from which the Collector seeks no advantage in No. 266, since he has stipulated (R. 296–297) that the oils there involved received a domestic processing prior to the effective date of the Act, and it is irrelevant to the claim of conflict between the Third and Seventh Circuits.

CONCLUSION

The instant petition presents questions wholly distinct from the single issue of statutory question involved in the Collector's petition in No. 266. The questions presented here were correctly decided by the court below, and there is no conflict. The petition should be denied.

Respectfully submitted.

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SEWALL KEY,
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OCTOBER 1943.

APPENDIX

Revenue Act of 1934, c. 277, 48 Stat. 680:

SEC. 602½. PROCESSING TAX ON CERTAIN OILS.

(a) There is hereby imposed upon the first domestic processing of coconut oil, sesame oil, palm oil, palm kernal[1] oil, or sunflower oil, or of any combination or mixture containing a substantial quantity of any one or more of such oils with respect to any of which oils there has been no previous first domestic processing, a tax of 3 cents per pound, to be paid by the processor. There is hereby imposed (in addition to the tax imposed by the preceding sentence) a tax of 2 cents per pound, to be paid by the processor, upon the first domestic processing of coconut oil or of any combination or mixture containing a substantial quantity of coconut oil with respect to which oil there has been no previous first domestic processing, except that the tax imposed by this sentence shall not apply when it is established, in accordance with regulations prescribed by the Commissioner with the approval of the Secretary, that such coconut oil (whether or not contained in such a combination or mixture), (A) is wholly the production of the Philippine Islands or any other possession of the United States, or (B) was produced wholly from materials the growth or production of the Philippine Islands or any other possession of the United States, or (C) was brought into the United States on or before the 30th day after the date of the enactment of this Act or produced from materials brought

[1] So in original.

into the United States on or before the 30th day after the date of enactment of this Act, or (D) was purchased under a bona fide contract entered into prior to April 26, 1934, or produced from materials purchased under a bona fide contract entered into prior to April 26, 1934. All taxes collected under this section with respect to coconut oil wholly of Philippine production or produced from materials wholly of Philippine growth or production, shall be held as a separate fund and paid to the Treasury of the Philippine Islands, but if at any time the Philippine Government provides by any law for any subsidy to be paid to the producers of copra, coconut oil, or allied products, no further payments to the Philippine Treasury shall be made under this subsection. For the purposes of this section the term "first domestic processing" means the first use in the United States, in the manufacture or production of an article intended for sale, of the article with respect to which the tax is imposed, but does not include the use of palm oil in the manufacture of tin plate.

* * * * *

Revenue Act of 1936, c. 690, 49 Stat. 1648:

SEC. 702. PROCESSING TAX ON CERTAIN OILS.

(a) The first sentence of section 602½ of the Revenue Act of 1934 is amended to read as follows:

"(a) There is hereby imposed upon the first domestic processing of coconut oil, palm oil, palm-kernel oil, fatty acids derived from any of the foregoing oils, salts of any of the foregoing (whether or not such oils, fatty acids, or salts have been refined, sulphonated, sulphated, hydrogenated, or otherwise processed), or any com-

bination or mixture containing a substantial quantity of any one or more of such oils, fatty acids, or salts, a tax of 3 cents per pound to be paid by the processor, but the tax under this section shall not apply (1) with respect to any fatty acid or salt resulting from a previous first domestic processing taxed under this section or upon which an import tax has been paid under section 601 (c) (8) of the Revenue Act of 1932, as amended, or (2) with respect to any combination or mixture by reason of its containing an oil, fatty acid, or salt with respect to which there has been a previous first domestic processing or upon which an import tax has been paid under such section 601 (c) (8)."

(b) Notwithstanding the provisions of subsection (a) of this section, the first domestic processing of sunflower oil or sesame oil (or any combination or mixture containing a substantial quantity of sunflower oil or sesame oil), if such oil or such combination or mixture or such oil contained therein was imported prior to the effective date of this title, shall be taxed in accordance with the provisions of section 602½ of the Revenue Act of 1934 in force on the date of the enactment of this Act.

Treasury Regulations 48, promulgated under the Revenue Act of 1934:

ART. 5. (as amended by T. D. 4695, XV–2 Cum. Bull. 324 (1936)). *Measure of the tax.*—(*a*) *Generally.*—The measure of the tax is the quantity of oil or oils (in pounds) put into process, that is, the amount of tax will be determined by the quantity of the oil or oils which, in any way, enters into the first domestic processing.

* * * * *

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